The Krygier Report

An exclusive newsletter from Mark J. Krygier, Vice President & Portfolio Manager | August 2017 www.krygierwealthmanagement.ca

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Are you a student of history?

Globally, the markets as well as many currencies, including our own "loonie", are once again giving investors the opportunity to reconsider their tolerance for fluctuation in their portfolios. It is a truism of human nature that we are creatures of habit and when we find ourselves in an uncomfortable situation we generally tend to react according to our past responses in similar circumstances. However, this habitual behaviour should give us a moment to pause, as to paraphrase the American philosopher George Santayana "Those who do not learn from history are doomed to repeat it." If we continually revert to certain behaviours in response to particular stimuli then we have in fact not learned the dangers of our past behaviours and we will instead be likely to repeat our past mistakes. For instance, an investor who found him or herself panicking, in what was absolutely a time of panic, during the 2008-09 financial crisis, and who as a result sold their investments at "fire sale prices", only to see the markets later stabilize and rebound, should have learned the danger of making decisions out of panic. The reality, to which hard-core smokers can attest, is that old habits are hard to kick.

A gentleman I know who is currently in his 70s, like many of his generation, used to smoke 2-3 packs of cigarettes a day back in the '80s. Despite his relatives regularly begging him to stop this deadly habit, and despite having tried many methods for quitting, including nicotine gum, etc., he was finally able to quit only once he went "cold turkey", i.e. complete abstinence. After several painful days of withdrawal the habit was kicked and he never resumed smoking. With a dangerous substance like tobacco, alcohol or drugs it is fairly easy to identify what habit one, at least conceptually, needs to quit, for the sake of one's long-term health benefits. However, with behaviors that may at times actually protect oneself from assuming risk with which one is not truly comfortable, it is a lot harder to identify which ones are destructive if repeated and which ones are in fact helpful. Perhaps the key to identifying which behaviours are worth changing and which are not, is to identify which are the ones that in the past resulted in long-lasting negative impacts on one's well-being. An investor who sold all or a significant part of his or her equity (stock) investments near the bottom of the last bear market (early 2009) suffered a real negative financial impact over the following decade, in trying to recover the losses "realized" during that time period. In contrast, most of the investors who held onto their investments during those tough times experienced a relatively short recovery period as their "paper" losses recovered in many cases in less than a year from the "bottom".

As investors, we are regularly being challenged to stick to our vision of what we want and need for ourselves. These challenges may come from financial companies promising a better version of whatever we are currently doing to manage our financial affairs, from news headlines ranting about reasons to panic or be exuberant, and from well-meaning friends or colleagues who have their own goals, aspirations and fears which may periodically project onto us as they tell us what we could be doing better. A well-balanced portfolio which is designed to provide a regular stream of dividend and interest income without impairing one's capital, and which ought to be able to do so in good times and in bad times barring a total collapse of the financial system, should in my mind be treated no differently than a rental property which is providing its owners with regular monthly income from its rental or lease payments, and whose value should increase over time. Just as the property owner would scoff at the idea of selling a low vacancy rental property when real estate prices are low, and would instead be more likely to look for other such properties to buy, so too should the stock investor scoff at the headline-fueled suggestion that one ought to sell at fire sale prices as long as the "tenants" are continuing to pay regular income.

In reality, it may be easier for the income-focused investor to stick with his or her investment plan as the income being generated becomes the focal point of investing. However, a primarily growth-oriented investor may be more likely to focus on all of the short-term bumps and grinds of the normal market fluctuations as they may believe they have nothing but "the returns" to show for their investing efforts. I believe it is imperative for the latter investor, who really doesn't need the income from his or her portfolio, to establish a reasonable benchmark by which to judge their portfolio and, perhaps even more importantly, they need to establish a reasonable time frame for judging its relative performance. Setting too tight a benchmark and too short a time frame can easily lead an investor into being "whip-sawed" into making poor investment decisions which they may later regret. Certainly, looking at portfolio valuations on a daily basis is mostly a useless exercise. On the other hand, ignoring one's investments entirely for a couple of years may also not be useful, as the likelihood is that many opportunities for improving one's investments will come along in between such reviews. The frequency of the reviews and the type of benchmarking should be practical and relevant to one's own individual long-term goals.

Bottom line

As an investor you do not need to pursue a PhD in history or psychology to gain insight into your expected behaviour during stressful times. Instead, focus on your own individualized long-term goals and where you stand in relation to them. Use those goals to establish relevant benchmarks and time frames to meet those goals. Finally, learn from your past reactions in different market environments to avoid repeating past mistakes!

Global benchmarks
As at July 31, 2017 (Canadian $ Returns)

Asset class	1 year	3 years	5 years
S&P/TSX Composite T/R (Canada)	6.8%	2.6%	8.6%
S&P 500 TR - US$	16.0%	10.9%	14.8%
NASDAQ Composite - US$	23.0%	13.3%	16.6%
MSCI Europe Index Price Return	11.4%	3.8%	10.9%
MSCI Emerging Markets	16.7%	4.6%	6.8%
China S.E Shanghai A Price Return	3.7%	16.0%	12.8%
MSCI World Index Price Return	8.9%	9.4%	14.3%

Asset class	1 year	3 years	5 years
30-year U.S. T-Bond - US$	-11.7%	5.3%	1.3%
10-year U.S. T-Bond - US$	-5.4%	2.8%	0.6%
Long GOC Bond (2048)	-14.7%	3.3%	1.6%
10-year GOC Bond	-6.6%	2.8%	2.0%
5-year GOC Bond	-3.3%	1.6%	1.6%
3-month CDN T-bill	0.5%	0.6%	0.7%
US$/CDN$ (1.2477)	-4.4%	4.6%	4.5%

Source: RBC Capital Markets Quantitative Research

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